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LAU KEAN LEONG v. LITS SOLUTIONS SDN BHD & ORS

HIGH COURT MALAYA, PULAU PINANG
AZMI ABDULLAH J
[ORIGINATING SUMMONS NO: PA-24NCVC-1174-12-2018]
25 JANUARY 2020

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COMPANY LAW: *Derivative action – Application for leave – Breach of fiduciary duties – Whether director had obligation to act in good faith and in best interests of company – Whether director put himself in position of conflict of interest – Whether director had taken corporate opportunity during his tenure as director and exploited business opportunities belonging to company – Whether applicant satisfied guidelines provided under s. 348(4) of Companies Act 2016 – Whether leave to commence derivative action ought to be allowed*

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COMPANY LAW: *Directors – Breach of fiduciary duties – Application for leave to commence derivative action – Whether director had obligation to act in good faith and in best interests of company – Whether director put himself in position of conflict of interest – Whether director had taken corporate opportunity during his tenure as director and exploited business opportunities belonging to company – Whether applicant satisfied guidelines provided under s. 348(4) of Companies Act 2016*

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The plaintiff and the second defendant were the only shareholders and directors of the first defendant ('LITS Solutions Sdn Bhd). Each of them owned 50% of the shares in the first defendant company. The first defendant's business was to market a smartphone application, Flexi Parking, which enables its users to pay for the parking charges without the need to purchase physical parking coupons, which is done by transferring pre-paid credit from the user's smartphone to the database at the local authorities. The third defendant was a company incorporated by the second defendant while being a director and shareholder of the first defendant. The third defendant was conducting the same line of business as that of the first defendant. Leave of the court was sought by the plaintiff to commence a derivative action under ss. 347 and 348 of the Companies Act 2016 ('Companies Act') against the second defendant for breach of his fiduciary duties to the first defendant in that, *inter alia*, he had (i) while still being a shareholder and director of the first defendant, incorporated the third defendant with the name 'Leading Innovative Technologies & Systems Sdn Bhd', the abbreviation of which is LITS (being the first defendant) to confuse the public and those who deal with the third defendant into thinking that they were in fact dealing with the first defendant when that was not the case. He had incorporated the third defendant without the knowledge, consent or approval of the plaintiff. The second defendant, as a director, owed fiduciary duties to the first defendant,

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which involved an obligation to act in a trustworthy manner, in good faith and honestly in the best interests of the first defendant. The second defendant had breached those fiduciary duties to the first defendant; (ii) while still being a shareholder and director of the first defendant, conducted business similar to that of the first defendant and in competition with the first defendant and had put himself in a position of conflict of interest and duty and had not acted in the best interests of the first defendant; (iii) claimed from the first defendant expenses incurred by him for the Shah Alam project but had instead channelled the said project to the third defendant; and (iv) taken corporate opportunity and so was in breach of his fiduciary duty during his tenure as a director. He exploited the business opportunities belonging to the first defendant and had used the third defendant to take the first defendant's business. Subsequently, the second defendant had tendered his resignation as the CEO (and not as the director) of the first defendant. It was the plaintiff's case that he had filed this action in good faith and not for personal vendetta and that he had satisfied the requirements for obtaining leave of this court to file the proposed action.

Held (granting leave application):

(1) The plaintiff, in satisfying the guidelines provided under s. 348(4) of the Companies Act, had fulfilled the conditions for bringing a derivative action and had *locus standi*. He was a complainant under s. 345 as he was a current member and also a director of the first defendant. The plaintiff, as the complainant, was acting in good faith and this was clear from the background facts in that his application for leave was *prima facie* made in the best interests of the company ('the first defendant'). His action was not frivolous or vexatious. There existed reasonable prospect for success in the anticipated derivative action. There was also reasonable and legitimate basis for bringing a derivative action to recover the loss of income which belonged to the first defendant. (paras 45-47 & 81)

(2) The conduct of the second defendant entitled the plaintiff to apply for leave to bring a statutory derivative action against the second and third defendants (a third party) because the second defendant had acted in breach of his fiduciary duties owed to the first defendant and gained personal benefit/enrichment from his wrongful actions against the first defendant. The plaintiff could bring action against the third defendant as the action was connected to and arose out of the second defendant's breach of his fiduciary duties. The plaintiff had a case for averring that the second defendant had breached his fiduciary duties to the company (the first defendant) in incorporating the third defendant and in diverting the business and business opportunities to the third defendant, in which he was, at all material times, the shareholder and director. If a loss of income arose from a breach of fiduciary duty on the part of a director, it would be in the interests of the company to take steps to recover such income. (paras 49, 50 & 81)

(3) The existence of financial benefit which the director had obtained personally through other companies, firms or businesses could be used to show that there was conflict of interest and duty. Further, a director owes a responsibility not to hide his interest or involvement in a transaction where the transaction is entered into by him for and on behalf of a third party in which he has an interest and the said third party competes with the company in respect of the business carried out by the company. The second defendant had obtained financial benefit through the third defendant which he had incorporated. When there is potential for conflict of interest and duty, the only way in which a director may retain the benefit he had obtained is by making full and frank disclosure to the general meeting and obtaining its approval. Herein, the second defendant had surreptitiously incorporated the third defendant and had diverted the business to the third defendant in which he was, at all material times, the shareholder and director. (paras 66 & 67)

(4) There would be a breach of duty in failing to avoid conflict of duty and interest if there was misappropriation, exploitation or diversion of business opportunities by a director in his own favour or in favour for an entity in which he had an interest (s. 218 of the Companies Act). This was what the second defendant had done. He had incorporated the third defendant and had diverted to the third defendant the business opportunity belonging to the first defendant. Corporate opportunity is a part of the company's information. The corporate opportunity/business which the second defendant had taken to the third defendant fell within the line of business of the first defendant and the first defendant was in a position to take the opportunity. The second defendant was actively seeking that business opportunity on behalf of the first defendant and he was aware of it. However, he wrongfully diverted that business to the third defendant and/or caused the business to be awarded to the third defendant which he had incorporated instead of to the first defendant. By way of the derivative action, the first defendant was entitled to seek, *inter alia,* an account of the profits made by the second defendant. (paras 69 & 80)

Case(s) referred to:

Aberdeen Railway Co v. Blaikie Bros (1854) 1 Macq 461 ***(refd)***
Abdul Rahim Suleiman & Anor v. Faridah Md Lazim & Ors [2017] 1 CLJ 633 CA ***(refd)***
Avel Consultants Sdn Bhd & Anor v. Mohd Zain Yusof & Ors [1985] 2 CLJ 11; [1985] CLJ (Rep) 37 SC ***(refd)***
Bhullar v. Bhullar [2003] BCLC 241 ***(refd)***
Celcom (Malaysia) Bhd v. Mohd Shuaib Ishak [2010] 7 CLJ 808 CA ***(refd)***
Cook v. Deeks [1916] 1 AC 554 ***(refd)***
Industrial Development Consultants Ltd v. Cooley [1972] 2 All ER 162 ***(refd)***
Ng Eng Ghee v. Mamata Kapildev Dave [2009] 3 SLR (R) 109 ***(refd)***
Ong Keng Huat v. Fortune Frontier (M) Sdn Bhd & Anor [2015] 10 CLJ 599 HC ***(refd)***

Pang Yong Hock and Another v. PKS Contracts Services Pte Ltd (2004) 3 SLR 1 ***(refd)***
PJTV Denson (M) Sdn Bhd & Ors v. Roxy (Malaysia) Sdn Bhd [1980] 1 LNS 55 FC ***(refd)***
Regal (Hastings) Ltd v. Gulliver and Others [1967] 2 AC 134 ***(refd)***
Tam Tak Chuen v. Eden Aesthetics Pte Ltd and Another (Khairul bin Abdul Rahman and Another, Non Parties) [2010] 2 SLR 667 ***(refd)***
The Board Of Trustees Of The Sabah Foundation & Ors v. Datuk Syed Kechik Syed Mohamed & Anor [1999] 1 LNS 36 HC ***(refd)***
Yukilon Manufacturing Sdn Bhd & Anor v. Dato' Wong Gek Meng & Ors (No 4) [1998] 4 CLJ Supp 319 HC ***(refd)***

Legislation referred to:
Companies Act 2016, ss. 218, 345, 347, 348(4)

For the plaintiff - A Suppiah; M/s Presgrave & Matthews
For the 2nd & 3rd defendants - H K Niah & Sivaram Prasad; M/s Christopher & Lee Ong

Reported by Suhainah Wahiduddin

JUDGMENT

Azmi Abdullah J:

Introduction

[1] Enclosure 1 is for leave to commence a derivative action against the second and third defendants under ss. 347 and 348 of the Companies Act 2016. The cause papers filed in respect of encl. 1 are as follows:

(i) notice of application dated 21 December 2018;

(ii) afidavit sokongan affirmed by Lau Kean Leong ("the plaintiff") on 21 December 2018;

(iii) afidavit jawapan affirmed by Lai Thiam Sin on 30 January 2019 for and on behalf of himself and the third defendant;

(iv) afidavit balasan affirmed by Lau Kean Leong on 25 February 2019;

(v) afidavit jawapan kedua affirmed by Lai Thiam Sin on 18 March 2019; and

(vi) afidavit balasan (2) plaintif affirmed by Lau Kean Leong on 8 April 2019.

[2] The prayers sought by the plaintiff under encl. 1 are, *inter alia*, as follows:

(i) that the plaintiff be granted leave to commence this action for and on behalf of the first defendant named above, being LITS Solutions Sdn Bhd or to bring this proceedings in the name of the first defendant for the benefit of the first defendant within 30 days from the date of this order against:

A (a) Lai Thiam Sin, the second defendant above-named, being the director of the first defendant and also the director of the third defendant;

(b) the third defendant, being Leading Innovative Technologies & Systems Sdn Bhd; and/or

B (c) any other party or person which/who is liable to the first defendant.

(ii) that leave be granted to the plaintiff to commence and/or bring and/or maintain proceedings, including any interlocutory applications, against the parties named above in the name of or the benefit of the first C defendant;

(iii) that leave be granted to the plaintiff to oppose in the name of and for the benefit of the first defendant, including but not limited to any application or interlocutory application filed for and/or on behalf of the second and third defendants above-named; and

D (iv) plaintiff is granted leave to control the conduct of the above proceedings, including giving instructions to the plaintiff's solicitors.

[3] Leave was granted after deliberating the written submissions and further oral clarifications by counsels of respective parties. Resulting from E the appeal filed by the second and third defendants, it is hereby furnished the reasons for the said decision of this court.

Parties Involved

[4] The plaintiff and the second defendant are the only shareholders and F directors of the first defendant (LITS Solutions Sdn Bhd). Each of them own 50% of the shares in the first defendant company. The SSM search on the first defendant is contained in exh. "LKL1" in Lau Kean Leong's affidavit-in-support dated 21 December 2018.

[5] The first defendant's business was to market a smartphone application G known as "Flexi Parking" application. The said application enables its user to pay for the parking charges without the need to purchase physical parking coupons. This is done by transferring pre-paid credit from the user's smartphone to the database at the local authorities.

[6] The third defendant is a company incorporated by the second H defendant while being a director and shareholder of the first defendant. The third defendant conducts the same line of business as that of the first defendant. The SSM search on the third defendant is found in exh. "LKL5" of Lau Kean Leong's affidavit-in-support dated 21 December 2018.

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Plaintiff''s Averments

[7] Leave of the court is sought by the plaintiff to commence a derivative action against the second defendant for breach of his fiduciary duties to the first defendant in that, *inter alia*:

(i) He had, while still being a shareholder and director of the first defendant, incorporated the third defendant with the name "Leading Innovative Technologies & Systems Sdn Bhd", the abbreviation of which is "LITS" (being the first defendant), to confuse the public and those who deals with the third defendant into thinking that they are in fact dealing with the first defendant when that is not the case. He had incorporated the third defendant without the knowledge, consent or approval of the plaintiff. The second defendant, as a director, owes fiduciary duties to the first defendant. Fiduciary duty involves an obligation to act in a trustworthy manner, in good faith and honest in the best interests of the first defendant. However, the second defendant has breached his fiduciary duties to the first defendant.

(ii) He had, while still being a shareholder and director of the first defendant, conducted business similar to that of the first defendant and in competition with the first defendant. He had thereby breached his fiduciary duties to the first defendant and put himself in a position of conflict of interest and duty and had not acted in the best interests of the first defendant.

(iii) He had claimed from the first defendant expenses incurred by him for the Shah Alam project but had instead channelled the said project to the third defendant.

(iv) He had taken corporate opportunity and so was in breach of his fiduciary duty during his tenure as a director. He exploited the business opportunities belonging to the first defendant. The third defendant was incorporated on 15 December 2016. He then used the third defendant to take the first defendant's business with Majlis Perbandaran Shah Alam. On 10 February 2017, he tendered his resignation as the CEO (and not as the director) of the first defendant.

(a) The Flexi Parking application was first marketed by the first defendant to Majlis Bandaraya Alor Setar, Kedah where the first defendant in collaboration with a company known as Kayangan Parking Sdn Bhd. Kayangan Parking Sdn Bhd introduced the said application for public parking bays in the city of Alor Setar. After the successful introduction of the Flexi Parking application in the city of Alor Setar, the first defendant expanded its business to the

State of Selangor. Majlis Perbandaran Sepang appointed the first defendant to manage its public parking through its concessionaire named Suasa Efektif (M) Sdn Bhd. The said Flexi Parking application was also introduced in Majlis Perbandaran Shah Alam, Subang Jaya, Sepang, Kepong, Kajang and other big cities in the State of Selangor.

(b) The second defendant took advantage of the business opportunities available to the first defendant and obtained personal benefit at the expense of the first defendant by diverting the said business opportunities, which he should have brought to the first defendant to which he owed fiduciary duties, to the third defendant and had prejudiced the business and interests of the first defendant and caused loss to the first defendant.

(c) The second defendant had taken up the said projects at a time when he was still a director of the first defendant. He resigned as the CEO of the first defendant on 10 February 2017, prompted or influenced by a desire to acquire the business opportunities sought by the first defendant. Directors who divert the business opportunity which the company had entrusted them with or for which they are responsible for acquiring on behalf of the company (and in which there was a real possibility that the contract could have been awarded to the company had the director not breached his duty), are liable to the company.

(v) He had used the information and know-how, including the patent rights of the first defendant, for his personal gain and had not acted in the best interests and for the proper purpose of the first defendant. The second defendant was the director for technology in the first defendant and developed the Flexi Parking application for the first defendant. He was drawing salary from the first defendant for developing the said application.

(vi) In view of the fiduciary nature of the relationship between the first defendant and the second defendant (the director), there are remedies available for the first defendant for breach of the directors' duty. The court can order him to compensate the first defendant for all the financial loss incurred by it or an account of profits he had made through the third defendant. The third defendant is a constructive trustee.

(vii) The plaintiff has filed this action in good faith and not for personal vendetta. There is merit in the plaintiff's application for leave. The plaintiff has satisfied the requirements for obtaining leave of this Honourable Court to file the proposed action.

Background Facts And Observations

[8] The first defendant was incorporated on 27 May 2014 by the plaintiff and the second defendant with the objective of marketing a product of the first defendant known as "Flexi Parking", which is now known as "Smart Parking". The abbreviation "LITS" is only coincidentally similar to the second defendant's name (Lai Thiam Sin). "LITS" is in fact the abbreviation for "Leading Innovative Technologies and Systems".

[9] The Flexi Parking system is a smartphone application which enables the user to make payment for public parking compared to the conventional parking system, which uses a car parking coupon. The said Flexi Parking system enables the user of the smartphone application to pay to the local authority for the public parking by purchasing credit provided under the said application.

[10] The plaintiff and the second defendant held discussions about the idea of Flexi Parking application prior to the first defendant being incorporated. Thereafter, the first defendant was incorporated. It was only then that the Flexi Parking application was developed. The Facebook was set up by the second defendant only after the said discussion and before the first defendant was formed. This shows that the second defendant had developed the Flexi Parking application for the first defendant and not for himself. In any event, by drawing salary from the first defendant for developing the said application, he had waived/abandoned any personal rights over the said application.

[11] The Flexi Parking system was introduced by the first defendant for the very first time in Alor Setar, Kedah whereby the first defendant together with a company known as Kayangan Parking Sdn Bhd introduced a system for the management of public car parking in Alor Setar ("the Alor Setar project"). Pages 21 to 26 (exh. "LKL2") in Lau Kean Leong's affidavit-in-support dated 21 December 2018 contain the documents relating to the Alor Setar project.

[12] After procuring the Alor Setar project and in order to further develop its business, the first defendant cooperated with a company known as Suasa Efektif Sdn Bhd. As a result of the said co-operation, Majlis Perbandaran Sepang appointed the first defendant, through Suasa Efektif Sdn Bhd (the concessionaire) to manage the public parking using the Flexi Parking system ("the Sepang project"). Pages 36 to 42 (exh. "LKL3") in Lau Kean Leong's affidavit-in-support dated 21 December 2018 contain the documents relating to the Sepang Municipal Council.

[13] After procuring the Sepang project, the second defendant, for and on behalf of the first defendant took steps to bid and/or to procure new projects, especially in Shah Alam, Selangor ("Shah Alam project") which has high market value compared to other markets. Pages 48 to 51 (exh. "LKL4") in Lau Kean Leong's affidavit-in-support contain the documents relating to the Shah Alam project.

[14] Thereafter, without the knowledge, approval or consent of the plaintiff, the second defendant discreetly incorporated a company known as "Leading Innovative Technologies & Systems Sdn Bhd" (the third defendant above-named) on 15 December 2016 and channelled the Shah Alam project to the third defendant. Exhibit "LKL5" in Lau Kean Leong's affidavit-in-support dated 21 December 2018 contains the SSM search on the third defendant.

[15] The agreement between the plaintiff and the second defendant during a meeting between them in January 2017 was that the new company to be incorporated by the second defendant will be appointed as an agent to collect charges for the transactions from Suasa Efektif Sdn Bhd and not to compete with the first defendant in any way whatsoever.

[16] The plaintiff had no knowledge that the second defendant had already incorporated the third defendant even before their meeting in January 2017. Neither did the second defendant informed the plaintiff that he had already incorporated the new company in the name of the third defendant. He had deliberately failed to disclose to the plaintiff the fact about the incorporation of the third defendant.

[17] The second defendant had made claims for expenses from the first defendant as showcased at pp. 65 to 225 (exh. "LKL6") in the plaintiff's affidavit-in-support dated 21 December 2018 containing the documents relating to the claims for expenses made by the second defendant to the first defendant. The claims include, *inter alia*, travelling expenses, handphone charges, breakfast, lunch, dinner, etc.

[18] The application for patent for the "Flexi Parking" filed by the second defendant was not approved by the authorities because there existed other prior similar applications. A copy of the status of the application for patent from "MyIpo" website is shown in p. 22 (exh. "LKL11") of the affidavit-in-reply of Lau Kean Leong dated 25 February 2019.

[19] The first plaintiff was a new company and whatever understanding which existed between the plaintiff and the second defendant was a loose arrangement wherein they both had responsibilities for developing the first defendant. The plaintiff too had knowledge about the technical development of computer software. The second defendant claims that he was responsible for technical matters. If so, the first defendant could not have been involved

merely in marketing. The Flexi Parking application was developed by the second defendant for the first defendant and it belonged to the first defendant. A copy of the WeChat communication in relation to patent and the quotation from Adastra to the first defendant through the second defendant is shown in exh. "LKL12" in Lau Kean Leong's affidavit-in-reply dated 25 February 2019.

[20] At the beginning, after the first defendant had been incorporated, the understanding between the plaintiff and the second defendant was that both of them would use their own equipment for the purpose of the first defendant because at that time the first defendant did not have sufficient funds to pay for the purchase of equipment. The plaintiff used his own funds to purchase computer and to fund the marketing activities of the first defendant.

[21] The understanding between the plaintiff and the second defendant at the time of incorporation of the first defendant was that they would get their salary only after procuring projects. All those involved in the first defendant had knowledge about it and understood that they were working *pro bono* until the first defendant obtained projects and developed strong financial standing. The initial understanding between the plaintiff and the second defendant was that each of them will pay for the costs relating to things purchased. The plaintiff too did not claim for the computer, for travelling, marketing and entertainment. The second defendant only purchased computer and handphone, which were not surrendered to the first defendant.

[22] Work which had been done by the second defendant for the first defendant was part of his responsibility to develop the first defendant in his capacity as a director of the first defendant. The plaintiff too played his part in developing the first defendant. He too went to Majlis Bandaraya Alor Setar ("MBAS") to make presentation and incurred expenses for that purpose. Second defendant had knowledge of the presentation made by the plaintiff to MBAS and he had prepared the demonstration application for that purpose using the logo of MBAS. Further, the second defendant had knowledge about the official launching by MBAS and had posted pictures in the Facebook for Flexi Parking. A copy of the image from the Flexi Parking Facebook is contained in exh. "LKL13" of Lau Kean Leong's affidavit-in-reply dated 21 December 2018.

[23] The presentation was done together with Alam Indah Sdn Bhd, which was the concessionaire for the management of parking in Penang Island. Alam Indah Sdn Bhd then was developing its own equipment and application called the "Smart Parking Gadget". As such, the said company was not interested in the Flexi Parking application of the first defendant.

[24] The Flexi Parking application had already been used in Alor Setar. If the first defendant needed active deployment only then will it need to employ software engineers and technicians. The technicians are needed for maintenance and not for the development of the Flexi Parking because the said application had already been developed and was available.

[25] In May 2014, the second defendant was still working and getting salary from a company named Altera Corporation. Exhibit "LKL21" in the affidavit-in-reply (2) of the plaintiff shows that the second defendant had conducted 50 training sessions since 2005. The said posting is from 14 August 2015 and it has been posted by Malaysian Global Innovation and Creativity Centre. The second defendant has knowledge about the said posting. Danny and Jack Lee were also the employees of the said company and were drawing their salary from the said company (Altera Corporation).

Exhibit "LKL14" in Lau Kean Leong's affidavit-in-reply dated 25 February 2019 contains a copy of the WeChat communication which shows that the second defendant had resigned from his position at Altera Corporation on his own volition.

[26] Pravinder Singh and Radin Hairi had not joined the first defendant in March 2015. Radin Hairi was the employee of Kayangan Parking Sdn Bhd (the concessionaire for parking in MBAS) until May 2015 and joined the first defendant only in June 2015. The second defendant has admitted in para. 18(b) of his affidavit-in-reply dated 30 January 2019 that he played the role of a director for technology and that Jack Lee played the role of software engineer in the first defendant. This shows that the Flexi Parking application had been developed for the first defendant and the role of the second defendant was not merely as the marketing agent in the first defendant as alleged by him.

[27] The second defendant had from time to time been the consultant for the said company for technical courses since 2011. A copy of the course outline for the courses taught by him as the consultant to Dream Catcher Consulting Sdn Bhd in 2011 is shown in exh. "LKL15" in Lau Kean Leong's affidavit-in-reply dated 25 February 2019.

[28] The plaintiff and the second defendant did not draw any salary in the initial period after incorporation of the first defendant as there wasn't sufficient funds in the first defendant. The second defendant had claimed the sum of RM12,136.08 for travelling, hotel accommodation, server, internet, handphone charges and other expenses, including for going to Selangor for dealings with Suasa Efektif Sdn Bhd in his capacity as the director of the first defendant.

[29] Although the first defendant did not have sufficient funds to pay, the plaintiff signed a cheque for RM12,136.08 to be paid to the second defendant on the understanding that the said cheque can be presented for payment only after receipt of RM10,000 from Suasa Efektif Sdn Bhd for the sale of four printing machines of the first defendant to Suasa Efektif Sdn Bhd. However, the second defendant had presented the said cheque before receiving the cheque from Suasa Efektif Sdn Bhd. This caused the second defendant to pay his own money into the first defendant's account in order to avoid the said cheque issued by the first defendant from being dishonoured. It was the only time when the second defendant had paid into the first defendant's account. The said payment was not for the purpose of investment in the first defendant.

[30] The second defendant had never injected funds to pay the sales employees of the first defendant. He also did not pay or invest any of the proceeds of the alleged sale of his condominium into the first defendant's account.

[31] The enhancement of the Flexi Parking application was a part of the responsibility of the second defendant in the first defendant because he was responsible for technical matters. He enhanced the said application for the first defendant and not for himself. As the second defendant was responsible for technical matters in the first defendant, he developed the Flexi Parking application as part of his responsibility to the first defendant. He has averred in his affidavit that the first defendant is an entity involved in marketing. If the first plaintiff had been incorporated merely for marketing activities, it would not have needed an officer responsible for technical matters.

[32] The Flexi Parking operation in Alor Setar was terminated in November 2015 as a result of Kayangan Parking Sdn Bhd being terminated of its services as the concessionaire for MBAS due to its failure to settle the monthly charges to MBAS. As such, the first defendant did not need any software engineer or technician to operate the Flexi Parking application there.

[33] The second defendant resigned from his post as the Chief Executive Officer of the first defendant on 10 February 2017 based on unreasonable grounds. Exhibit "LKL8" in Lau Kean Leong's affidavit contains the second defendant's resignation letter. He resigned on his own volition and it is not reasonable to blame the first defendant for lack of contracts as the first defendant was a new company.

[34] The second defendant's allegation that he had created the Facebook for marketing the Flexi Parking application on 19 April 2015 cannot be true as the first defendant was incorporated only on 19 April 2015. The plaintiff too continued with his Flexi Parking marketing activities for the local authorities

and made presentation to Majlis Bandaraya lpoh and Majlis Bandaraya Melaka. A copy of the letter from the said local authorities and the photographs showing the presentations are contained in exh. "LKL16" of Lau Kean Leong's affidavit-in-reply dated 25 February 2019.

[35] The filing of tax returns and audited report for the first defendant is the joint responsibility of the plaintiff and the second defendant. However, the second defendant failed to forward a complete set of the receipts relating to his claims to the plaintiff even until this action was filed. The delay in the filing of the tax returns for the first defendant was due to the failure on the part of the second defendant to send the said receipts.

[36] The reason given by the second defendant for the need to get the licence from the Ministry of Finance ("MOF") cannot be true. Firstly, the licence from MOF was not needed at that time because the first defendant's contract was with a private company until December 2016 and not with the Government. Secondly, the MBAS and Sepang projects had become operational without the MOF licence.

[37] The second defendant claims that he left the first defendant because it had no MOF licence; it had not filed the tax returns and audit report and he was not paid any salary. These allegations cannot be a ground for breaching his fiduciary duties to the first defendant. The actions of the second defendant had caused the first defendant in not obtaining any income to pay for the secretarial services and other services. In 2017, the plaintiff had to use his own money to pay although the second defendant is the owner of 50% of the shares in the first defendant. The tax returns could not be filed because there were no funds in the first defendant and also because there were no proper documents from the second defendant. The actions of the second defendant show that he wanted the first defendant to go into insolvency in order to justify his action in forming the third defendant.

[38] The understanding between the second defendant and the plaintiff was that the patent for Flexi Parking will be filed under the first defendant but the second defendant breached the said understanding. Exhibit "LKL12" in the affidavit-in-reply dated 25 February 2019 is referred.

[39] The investors had invested the sum of RM800,000 and thereafter advanced the sum of RM65,000 based on the promise of getting 20% of the shares in the first defendant. A copy of the letter from the investor and a cheque image for RM865,000 are shown at pp. 41 to 47 (exh. "LKL17") in Lau Kean Leong's affidavit-in-reply dated 25 February 2019. The first defendant would not have funds if there was no investor. The funds of the first defendant was not contributed by the second defendant. All the cheques were paid into the first defendant's account in CIMB which required the signature of the plaintiff and the second defendant. If the existence of investor sis denied, how could he have obtained salary and made claims for his expenses.

[40] The first defendant was not able to make payment online for the Alor Setar project because the concessionaire, being Kayangan Parking Sdn Bhd, did not want to give consent to the first defendant to do so. The revenue was lesser than what had been expected because of the delay in using the new technology in Kedah which is considered as rural compared to the State of Selangor. Cheques collected from the customers were banked into the first defendant's account. The bad press was due to the dispute between the concessionaire and MBAS and as such they were not able to redeem the credit because MBAS had terminated the contract of Kayangan Parking Sdn Bhd.

[41] There is admission by the second defendant that the first defendant was the company which had been appointed for development of the Flexi Parking application and the role of the first defendant was not merely as the agent for marketing. If the second defendant's stand is that the first defendant was only involved in marketing, he would not have incurred development costs.

[42] The agreement between the plaintiff and the second defendant was to self-fund at the initial stage until investment was obtained. The plaintiff too used his funds for the costs of marketing. However, when the project was procured, the plaintiff did not divert it to a new company. The second defendant had enjoyed the proceeds from the Alor Setar project by drawing his salary and he also claimed the costs of purchase of handphones, server and printing machine which he used for running the system. The matter relating to finance of the first defendant was the joint responsibility of the plaintiff and the second defendant.

[43] The plaintiff would not have approved the second defendant's claims on 21 December 2016 if he had known that the second defendant had already incorporated the third defendant and had diverted the Flexi Parking contracts from Majlis Perbandaran Sepang, Shah Alam, Selayang and others to the third defendant. This shows that the plaintiff did not know that the second defendant had incorporated the third defendant. Further, the plaintiff had attended the launching ceremony of Flexi Parking for Majlis Bandaraya Shah Alam on 25 January 2017. If the plaintiff had known or was aware that the Majlis Bandaraya Shah Alam contract had been diverted by the second defendant to the third defendant in which he did not own any shares, he would not have attended that ceremony. Although the Alor Setar project had failed, it gave confidence to the other local authorities in Selangor to use the Flexi Parking system.

[44] A notice under s. 348 of the Companies Act 2016 dated 21 November 2018 has been served on the second defendant in his capacity as a director of the first defendant in relation to the plaintiff's intention of making this application and thereafter to file the proposed action. Exhibit "LKL10" in

A Lau Kean Leong's affidavit dated 21 November 2018 contains the said notice, receipt whereof the second defendant has acknowledged. The reply from the second defendant's solicitors dated 10 December 2018 has been replied by the plaintiff's solicitors as shown in exh. "LKL19" in Lau Kean Leong's affidavit dated 25 February 2019.

B **Legal Principles Applicable**

[45] The plaintiff has fulfilled the conditions for bringing a derivative action. He has *locus standi* and has satisfied the guidelines provided under s. 348(4) of the Companies Act 2016.

C **[46]** He is a complainant under s. 345 of the Companies Act 2016 as he is a current member and also a director of the first defendant. He has given 30 days' notice in writing to the second defendant (a director of the first defendant) of his intention to apply for the leave of court under s. 347 of the Companies Act 2016.

D **[47]** He, as the complainant, is acting in good faith and this is clear from the background facts elaborated above in that his application for leave is *prima facie* made in the best interests of the company (the first defendant).

[48] The plaintiff is acting in good faith and there is justification for bringing the derivative action as:

E

(i) He is a current shareholder and is seeking the recovery of the funds which will increase the value of his shares.

(ii) He has legitimate interest in the welfare and management of the first defendant.

F

(iii) He has a right not to allow another equal shareholder and director of the first defendant (that is, the second defendant) to act to the detriment of the first defendant's and his interests by diverting to the third defendant the business and business opportunities which should have come to the first defendant.

G

[49] The conduct of the second defendant entitles the plaintiff to apply for leave to bring a statutory derivative action against the second and third defendants (a third party) because the second defendant has acted in breach of his fiduciary duties owed to the first defendant and gained personal benefit/enrichment from his wrongful actions against the first defendant.

H

[50] The plaintiff can bring action against the third defendant as the action is connected to and arises out of the second defendant's breach of his fiduciary duties. The second defendant has benefitted from the third defendant.

I

(i) Section 347 of the Companies Act 2016:

347 Derivative proceedings

(1) A complainant may, with the leave of the Court initiate, intervene in or defend a proceeding on behalf of the company.

(2) Proceedings brought under this section shall be brought in the company's name.

(3) The right of any person to bring, intervene in, defend or discontinue any proceedings on behalf of a company at common law is abrogated.

(ii) Section 348 of the Companies Act 2016:

348 Leave of Court

(1) An application for leave of the Court under section 347 shall be made to the Court without the need for an appearance to be entered.

(2) The complainant shall give thirty days' notice in writing to the directors of his intention to apply for the leave of court under section 347.

(3) Where leave has been granted for an application under section 347, the complainant shall initiate proceedings in Court within thirty days from the grant of leave.

(4) In deciding whether or not leave shall be granted, the Court shall take into account whether:

(a) the complainant is acting in good faith; and

(b) it appears *prima facie* to be in the best interest of the company that the application for leave be granted.

(5) Any proceedings brought, intervened in or defended under this section shall not be discontinued, compromised or settled except with the leave of the Court.

(iii) Section 345 of the Companies Act 2016:

345 Interpretation

For the purposes of this Division, "complainant" means:

(a) a member of a company, or a person who is entitled to be registered as a member of a company;

(b) a former member of a company if the application relates to the circumstances in which the member ceased to be a member;

(c) any director of a company; or

(d) the Registrar, in the case of a company declared under section 590.

[51] The plaintiff is acting in good faith in seeking leave to commence a derivative action. The court shall assume that the plaintiff, who is coming to court with a reasonable and legitimate claim, is acting in good faith unless proven otherwise. In this case, the second defendant has the burden of proving that the plaintiff is not acting in good faith.

[52] In *Pang Yong Hock and Another v. PKS Contracts Services Pte Ltd* (2004) 3 SLR 1 it was decided:

> 17. *Agus Irawan v. Tho Teck Chye* (2002) 2 SLR 198 involved a director of a company applying for leave under s. 216A of the Companies Act to commence an action against two other directors of the company for alleged breach of fiduciary duties. Choo Han Teck JC (as he then was) dismissed the application. In responding to an application to file a further affidavit and to have the plaintiff there cross-examined, the judge said (at 6):
>
> > I do not see any need to expand or broaden the case at this stage. At this stage the court need not and ought not be drawn into an adjudication on the disputed facts. This is what a *prima facie* legitimate or arguable case is all about. Leave to cross-examine in such situations ought to be sparingly granted. I need only consider the grounds and points of challenge raised by the defendants to see if they are sufficient in themselves to destroy the credibility of the plaintiff's propounded case without a full scale hearing to determine who was truthful and who was not.
>
> Agreeing with the approach taken by Lai J in the earlier case of *Teo Gek Luang v. Ng Ai Tiong*, Choo JC went on to say (at [8] that the terms "legitimate" and "arguable" must be given their common and natural meaning, which was that the claim must have a reasonable semblance of merit, "not that it is bound to succeed or likely to succeed, but that if proved the company will stand to gain substantially in money or money's worth".
>
> Addressing the company's argument that the burden was on the plaintiff to prove that he acted in good faith, Choo JC said (at [9]):
>
> > If at all, the burden would be on the opponent to show that the applicant did not act in good faith; for I am entitled, am I not, to assume that every party who comes to court with a reasonable and legitimate claim is acting in good faith – until proven otherwise ... It would appear, in my view, that this requirement overlaps in no small way with the requirement that the claim must be in the interests of the company. Beyond that, whether malice or vindictiveness of the applicant ought to be taken into account must be left to the touch and feel of the court in each individual case ...

> This decision proceeded on appeal (Civil Appeal No 30 of 2002) and was dismissed by the Court of Appeal on 13 September 2002 with no written grounds of decision rendered.
>
> 19. In our opinion, the approach taken in the two cases above is generally beyond reproach ...

[53] The cited case of *Pang Yong Hock and Another v. PKS Contracts Services Pte Ltd* (*supra*) shows that the existence of hostility, dislike, acrimonious relationship or other personal reasons do not mean that the court will not grant leave as some of these elements are bound to exist between parties who cannot see eye to eye.

[54] In *Celcom (Malaysia) Bhd v. Mohd Shuaib Ishak* [2010] 7 CLJ 808; [2011] 3 MLJ 636 it was held:

> In considering whether the plaintiff was acting in good faith in accordance with s. 181B(4)(a), the court stated that the "test of good faith is two-fold. One is an honest belief on the part of the respondent and two, that this application is not brought up for a collateral purpose".
>
> The Court [at p. 649] referred to *Swansson v. RA Pratt Properties Pty Ltd & Anor* (2002) NSWSC 583:
>
> > ... in my opinion, there are at least two interrelated factors to which the courts will always have regard in determining whether the good faith requirement of s. 237(2)(b) is satisfied. The first is whether the applicant honestly believes that a good cause of action exists and has a reasonable prospect of success. Clearly, whether the applicant honestly holds this belief would not simply be a matter of bald assertion: the applicant may be disbelieved if no reasonable person in the circumstances could hold that belief. The second factor is whether the applicant is seeking to bring the derivative suit for such a collateral purpose as would amount to an abuse of process.

[55] The fact that the plaintiff will derive personal benefit from the derivative action does not necessarily mean that he lacks good faith or that he is not acting in the best interests of the company. If the derivative action is successful, the value of the plaintiff's shareholding will increase. Likewise, the company's assets/funds will increase with successful recovery of the funds which should have come to it but for the diversion of business and business opportunities by the second defendant in this case.

[56] The statutory derivative action is an application for leave to act for and on behalf of the company, that is, the leave application is brought on behalf of the company. At the leave stage:

A (i) The court should only consider the affidavit evidence filed by the parties and should not go into the merits of the case.

(ii) The court should only see whether the application for leave is frivolous. At the leave stage, the issue is only whether it is in the best interest of the company to pursue the claim.

B

[57] As stated in *Abdul Rahim Suleiman & Anor v. Faridah Md. Lazim & Ors* [2017] 1 CLJ 633; [2016] 6 MLJ 449 (CA).

> ... We need only say on this aspect that firstly, the court, in an application for leave, should not go into the merits of the case at the leave stage. Its
C role is to see if the application for leave is frivolous (*Tang Kwor Ham & Ors v. Pengurusan Danaharta Nasional Bhd & Ors* [2006] 5 MLJ 60). Secondly, in the matter of an application for leave under s. 181A of the Act, it would be the duty of the court to weigh all the circumstances and decide whether the claim ought to be pursued.
>
> At the leave stage, the issue is only whether it is in the best interest of
D the eighth respondent to pursue the claim ...

[58] The purpose for bringing the derivative action will determine whether the plaintiff is acting in good faith. In *Ong Keng Huat v. Fortune Frontier (M) Sdn Bhd & Anor* [2015] 10 CLJ 599; [2015] 11 MLJ 604:

E [46] ... Good faith was stated to be less dependent on the motives which trigger the application, but more on the purpose of the proposed derivative action, which must have a clear nexus with the company's benefits or interests. The motivations of the applicant would only amount to lack of good faith if they revealed that the applicant's judgment was influenced by purely personal considerations. The
F applicant must demonstrate that he is genuinely aggrieved and that his collateral purpose is sufficiently consistent with the objective of doing justice to the company.

(1) The first question to be determined was whether the plaintiff fell within the concept of a 'complainant' who sought leave to
G bring an action on behalf of and in the name of the company, as described under s. 181A(4) of the Act. The plaintiff as a director of the first defendant company fulfilled the requirement of s. 181A(4)(c) which refers to any director of a company.

(2) The plaintiff had on balance of probabilities established good faith in accordance with s. 181B(4)(a). The plaintiff honestly
H believed that a good cause of action existed and had a reasonable prospect of success. There was no evidence that the intended suit was instituted for a collateral purpose.

I

(3) The presence of a private interest cannot necessarily negate good faith if the same coincides with that of the company, especially given the shareholding structure of the company, and equally importantly, whether an analysis of the entire circumstances of the case establishes other evidence to suggest otherwise.

(5) The second defendant did not appear to demonstrate a conduct consistent with that expected of a responsible director and fiduciary of a company when facing the situation, choosing instead for a deadlock and worse still favouring a position that could expose himself to an allegation of breach of duty for conflict of interest.

[59] In *Tam Tak Chuen v. Eden Aesthetics Pte Ltd and Another (Khairul bin Abdul Rahman and Another, Non Parties)* [2010] 2 SLR 667, the court granted the application to commence derivative proceedings and dismissed the winding-up applications.

(2) Second, Dr Tam was acting in good faith by bringing the Application. On the facts, the main motivation for the Application was financial, not personal, and the beneficiaries of the action would be EA and EH and their shareholders who included Dr Khairul himself. The transfer of business from EA and EH to KAR could be legitimately questioned as it had a serious financial impact on EA and EH, and Dr Tam's desire to challenge Dr Khairul's actions could not be ascribed only to personal considerations. Indubitably, a loss of income was not be beneficial to a company and if that loss arose from a breach of fiduciary duty on the part of a director, it would be in the interests of the company to take steps to recover such income.

(3) Third, the Application had to appear to be *prima facie* in the interests of the companies. What this meant was that the Application had to be in the interest of the shareholders and could not appear to be frivolous or vexatious. Further, the court had to be satisfied that there was some reasonable basis for the underlying cause of action and that the Application was a legitimate one which could reasonably succeed. In all the circumstances of this case, the commencement of derivative proceedings against Dr Khairul and KAR was more beneficial to EA and EH than the remedy of winding up would have been.

[60] A director stands in a fiduciary relationship to the company. As such:

(i) He has a duty to act *bona fide* in the interests of his company and he must exercise his powers for the legitimate purposes of the company. Implicit in this relationship is his duty to avoid conflict between his personal interest and his duty to the company. This no-conflict rule is a fundamental fiduciary duty of a director.

A (ii) He should not make any profit from his position as a director. This is known as no-profit rule.

(iii) He should not take advantage of his position or use information which he has acquired while being a director, for his personal benefit. In short, he should not make any personal gain from the use of corporate
B opportunities. This is known as the no-misappropriation rule.

[61] The precedent of *Regal (Hastings) Ltd v. Gulliver and Others* [1967] 2 AC 134 held:

In *Aberdeen Ry Co. v. Blaikie Bros*, the headnote reads:

C
> The director of a railway company is a trustee, and, as such, is precluded from dealing, on behalf of the company, with himself, or with a firm of which he is a partner.

Lord Cranworth LC said:

D
> A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such agents have duties to discharge of a fiduciary nature towards their principal. And it is a rule of universal application that no one having such duties to discharge shall be allowed to enter into
E engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect.
>
> … The rule of equity which insists on those, who by use of a fiduciary position to make a profit, being liable to account for that
F profit, in no way depends on fraud, or absence of *bona fides;* or upon such questions or considerations as whether the profit would or should otherwise have gone to the plaintiff, or whether the profiteer was under a duty to obtain the source of the profit for the plaintiff, or whether he took a risk or acted as he did for the benefit of the plaintiff, or whether the plaintiff has in fact been
G damaged or benefited by his action. The liability arises from the mere fact of a profit having, in the circumstances, been made. The profiteer, however honest and well intentioned, cannot escape the risk of being called upon to account.
>
> I have no hesitation in coming to the conclusion, upon the facts of this case, that these shares, when acquired by the directors, were
H acquired by reason and only by reason of the fact that they were directors of Regal, and in the course of their execution of that office.

I

> In the result, I am of the opinion that the directors standing in a fiduciary relationship to Regal in regard to the exercise of their powers as directors, and having obtained these shares by reason and only by reason of the fact that they were directors of Regal and in the course of the execution of that office, are accountable for the profits which they have made out of them. The equitable rule laid down in *Keech v. Sandford and Ex parte Jame*s and similar authorities applies to them in full force. It was contended that these cases were distinguishable by reason of the fact that it was impossible for Regal to get the shares owing to lack of funds, and that the directors in taking the shares were really acting as members of the public. I cannot accept this argument. It was impossible for the *cestui que* trust in *Keech v. Sandford* to obtain the lease, nevertheless the trustee was accountable. The suggestion that the directors were applying simply as members of the public is a travesty of the facts. They could, had they wished, have protected themselves by a resolution (either antecedent or subsequent) of the Regal shareholders in general meeting. In default of such approval, the liability to account must remain.

[62] The facts of the Supreme Court case of *Avel Consultants Sdn. Bhd & Anor v. Mohd Zain Yusof & Ors* [1985] 2 CLJ 11; [1985] CLJ (Rep) 37; [1985] 2 MLJ 209 (SC) are similar to the case before this Honourable Court.

> The law is clear that a director of a company is in fiduciary relationship with his company and as such he is precluded from acting in a manner which will bring his personal interest into conflict with that of his company. Clearly the formation of Perunding AJZ was carefully planned. The firm is not only a rival of AVEL and ELMEC of which at the material time the Respondents were directors. It obtained the very job which was AVEL's job. Not only that, the firm canvassed for work from AVEL's and ELMEC's established clients, Kontena Nasional Sdn. Bhd and there is even evidence to show that the Respondents engineered the resignations of the key personnel on Channel Three project. This is borne out by the evidence that the first Respondent purporting to act as AVEL's managing director informed STMB of the pending resignation of these personnel some three months before the personnel handed in their resignation letters. The result of this notification was at the expense of AVEL which lost the job with the corresponding benefit to Perunding AJZ which gained it ... .

[63] *The Board Of Trustees Of The Sabah Foundation & Ors v. Datuk Syed Kechik Syed Mohamed & Anor* [1999] 1 LNS 36; [1999] 6 MLJ 497 is another relevant precedent. According to the facts of this case, on 15 April 1976, the Government headed by Tun Mustafa was voted out of office. Datuk Syed Kechik ("DSK") resigned as the director of Sabah Foundation. The timber licence of Banita was cancelled by the Government on 6 August 1976. Banita had been incorporated by DSK in the name of nominees for the purpose of

receiving a special timber licence. Banita was able to obtain the licence for a timber area due to information that DSK received as a director of Sabah Foundation and/or managing director of Sabah Foundation's subsidiary, Seranum. He had deliberately failed and neglected to make any disclosure of his control of and beneficial interest in Banita.

[64] The plaintiffs alleged that DSK was guilty of a fraudulent and dishonest design and acted in breach of his fiduciary duty as director and subsequently trustee of Sabah Foundation and as managing director of Seranum in that: (i) he failed in his entrusted duty to cause the whole of the surrendered area to be given to Sabah Foundation or Seranum; (ii) he made use of the opportunity and knowledge acquired by him as fiduciary agent of the plaintiffs to make profit for himself and Banita to the detriment of Sabah Foundation; and (iii) he fraudulently concealed from the trustees of Sabah Foundation and board of directors of Seranum the fact Banita had applied for and been granted a licence over the Wallace Bay area and he failed to disclose his control and financial interest in Banita.

[65] The High Court held that there was conflict of interest in the position of Datuk Syed Kechik (DSK) when considered in relation to his duty to the Sabah Foundation and some companies which he effectively controlled:

> (3) There was no doubt that DSK owed fiduciary duties to Sabah Foundation and Seranum, being respectively the director and managing director. DSK was a fiduciary. Those positions were well recognized as giving rise to a fiduciary relationship. But it does not mean that anything he did which may be a breach of duty amounted to a breach of fiduciary duty. Therefore, the mere fact that DSK was respectively the director and managing director of Sabah Foundation and Seranum did not mean that every duty of his was of a fiduciary nature. What must be determined was the obligations DSK owed as a fiduciary and in what respect he had failed to discharge those obligations.
>
> (4) The obligations of DSK were to be determined in relation to the area of 12 concessionaires and more particularly the Wallace Bay area. As soon as the government had evinced an intention through the cabinet decision and letters to give to Sabah Foundation or its group those areas, DSK would be expected to protect the interest of Sabah Foundation or its group. As soon as the Wallace Bay area was given to Banita instead of Sabah Foundation or its group, that completed the breach of duty on the part of DSK.
>
> (5) It was difficult to see, given the scope of DSK's duties as the director and managing director respectively of Sabah Foundation and Seranum, how the act of the Wallace Bay area being shanghaied by Banita could be anything but the result of a breach of fiduciary duty on the part of DSK. Therefore, the plaintiffs had

established that DSK had failed in his duty to cause the whole of the surrendered area to be given to Sabah Foundation or Seranum. The facts of the present case satisfied the tests which evolved from the three rules governing a trustee, *viz*: (i) the no profit rule; (ii) the no conflict rule; and (iii) the misuse of trust knowledge rule. Firstly, DSK had obtained benefit by reason and in the course of his office as a director. Secondly, by submitting the application for the licence which evinced his interest in the Wallace Bay area, DSK was in actual conflict with the interest of Sabah Foundation. Thirdly, right from the beginning DSK was made aware that the areas to be taken back from the 12 concessionaires were for the purposes of Sabah Foundation and any information relating to those areas was trust information.

(6) It was impossible not to conclude in this case that the Wallace Bay area and its timber licence came from or by reason or by means of the fiduciary position of DSK. The causal relationship between the act of DSK or Banita and the loss of the Wallace Bay by Sabah Foundation was established. Thus the plaintiffs were entitled to restitutionary remedy, ie accounting to Sabah Foundation and Seranum the profit derived from the Wallace Bay area; and compensatory relief, ie the loss consequent upon the cancellation of the licence.

[66] The existence of financial benefit which the director has obtained personally through other companies, firms or business can be used to show that there is conflict of interest and duty. Further, a director owes a responsibility not to hide his interest or involvement in a transaction where the transaction is entered into by him for and on behalf of a third party in which he has an interest and the said third party competes with the company in respect of the business carried out by the company. In the case before this court, the second defendant has obtained financial benefit through the third defendant which he had incorporated.

[67] When there is potential for conflict of interest and duty, the only way in which a director may retain the benefit he has obtained is by making full and frank disclosure to the general meeting and obtaining its approval. In the case before the court, the second defendant had surreptitiously incorporated the third defendant and had diverted the business to the third defendant in which he was at all material times the shareholder and director.

[68] Section 218 of the Companies Act 2016 prohibits a director, without the consent or ratification of a general meeting to use the property of the company, use any information acquired by virtue of his position as a director of the company or use any opportunity of the company which he became aware of, in the performance of his functions as the director of the company or engage in business which is in competition with the company to gain directly or indirectly, a benefit for himself or any other person, or cause detriment to the company.

[69] There will be breach of duty in failing to avoid conflict of duty and interest if there is misappropriation, exploitation or diversion of business opportunities by a director in his own favour or in favour of an entity in which he has an interest. This is provided for in s. 218 of the Companies Act 2016. This is also what the second defendant in this case has done. He has incorporated the third defendant and has diverted to the third defendant the business opportunity belonging to the first defendant. Corporate opportunity is a part of the company's information. The corporate opportunity/business which the second defendant has taken to the third defendant falls within the line of business of the first defendant and the first defendant was in a position to take the opportunity. The second defendant was actively seeking that business opportunity on behalf of the first defendant and he was aware of it. However, he wrongfully diverted that business to the third defendant and/or caused the business to be awarded to the third defendant which he had incorporated instead of to the first defendant.

[70] In *Cook v. Deeks* [1916] 1 AC 554, three directors of a company carrying on the business of railway construction contractors obtained a contract in their own names to the exclusion of the company. The contract was obtained under circumstances which amounted to a breach of trust by the directors and constituted them trustees of its benefits on behalf of the company. By their votes as holders of three-quarters of the issued shares they subsequently passed a resolution at a general meeting of the shareholders declaring that the company had no interest in the contract.

Held: The benefit of the contract belonged in equity to the company, and the directors could not validly use their voting power to vest it in themselves.

[71] The directors had breached their duty by placing their personal interests, which involved taking a corporate opportunity, being the right to build the new railway line, above their duty to their company.

[72] Meanwhile in *Bhullar v. Bhullar* [2003] BCLC 241 the company was involved in property development and the acquisition of an adjoining property by the directors was held to be a breach of the fiduciary duty and a diversion of corporate opportunity. The fact that other directors who were not in breach had indicated that they did not want the company to acquire any other property was held to be irrelevant to the finding of liability. It was also immaterial that the members of the company were already in negotiations to wind up the company. The court applied the strict fiduciary duty laid down in the case of *Regal (Hastings) Ltd v. Gulliver* (*supra*).

> The rule that a fiduciary was not allowed to enter into engagements in which he had, or could have, a personal interest conflicting, or which might possibly conflict, with the interests of those whom he is bound to protect was universal and inflexible. The test was whether "reasonable men looking at the facts would think there was a real sensible possibility of conflict" and where a fiduciary, such as the director of a company, exploited a commercial opportunity for his own benefit, the relevant question was not whether the party to whom the duty was owed (ie, the company) had some kind of beneficial interest in the opportunity but whether the fiduciary's exploitation of the opportunity was such as to attract the application of the rule. Since the only capacity in which the appellants carried on business was as directors of the company, in which capacity they were in a fiduciary relationship with the company, and since at the material time the company was still trading and acquisition of the property would have been commercially attractive to the company, the appellants were under a duty to communicate the existence of the opportunity to acquire the property to the company. Applying the test that "reasonable men looking at the facts would think there was a real sensible possibility of conflict", the appellants had acted in breach of their fiduciary duty to the company.

[73] In *Aberdeen Railway Co v. Blaikie Bros* [1854] 1 Macq 461, Aberdeen Railway Co entered into a contract to purchase equipment from a partnership named Blaikie Bros. The chairman of the board of Aberdeen Railway did not tell the other directors that he was a managing partner in the partnership form of Blaikie Bros. It was held as follows:

> It is the duty of a director of a company so to act as best to promote the interests of the company. That duty is of a fiduciary character, and no one who has such duties to discharge can be allowed to enter into engagements in which he has, or can have, a personal interest which conflicts, or possibly may conflict, with the interests of the company. A director, therefore, is precluded from entering on behalf of the company into a contract with himself or with a firm or company of which he is a member, and so strictly is this principle adhered to that no question can be raised as to the fairness or unfairness of a contract entered into.

[74] In *Ng Eng Ghee v. Mamata Kapildev Dave* [2009] 3 SLR (R) 109 it was held:

> It is important to note that these proscriptive duties are targeted against potential (not merely actual) conflict. A fiduciary should not even contemplate procuring a personal advantage, let alone secure one. The law has thus focused essentially on whether the performance of a duty by the fiduciary may be influenced or tainted by a conflict of interest. As it is virtually impossible to know what considerations have gone into an act or a decision of the fiduciary, the law sensibly does not require proof of an actual conflict of interest where such an allegation is made. The law only requires that there is a reasonable perception of a conflict of interest arising, since it is impossible to conduct an inquiry into the subjective motives which influenced a fiduciary's conduct to determine whether a genuine conflict of interest occurred.

[75] Any property belonging to the company is the company's property and cannot be used without the company's approval as decided in *Yukilon Manufacturing Sdn Bhd & Anor v. Dato' Wong Gek Meng & Ors (No 4)* [1998] 4 CLJ Supp 319. In this case the plaintiffs applied for an injunction against the first, second and fourth defendants from continuing to manufacture and offer for sale cosmetic sponge products and other products similar to or resembling the first plaintiff's and third defendant's products. The first and second defendants, while being the director of the first plaintiff and third defendant, had incorporated the fourth defendant and used it to compete directly with the business of the first plaintiff.

> [4] Both the 1st and 2nd defendants were in a fiduciary position and their liability to account did not depend upon proof of *mala fides*. The rule of equity is that generally one who owes a fiduciary duty is not allowed to enter into engagements which give rise to a conflict of interest. Both the 1st and 2nd defendants committed breach of fiduciary duties and trusts.
>
> [5] By diverting business from the 3rd defendant to the 4th defendant, both the 1st and 2nd defendants had unlawfully used their powers and undermined the 3rd defendant. ... As trustees, they did not act in the best interests of the 1st plaintiff and the 3rd defendant.

[76] A director's liability to the company does not depend on the company's inability or lack of capacity. As decided in the case of *Regal (Hastings) Ltd v. Gulliver*, the fact that the company could not exploit the transaction does not justify the director's conduct in exploiting the company's lack of capacity and obtaining the business for himself or an entity incorporated by him.

[77] Apart from the duty to avoid conflict of interest, there is also a prohibition that directors should not make secret profit out of their position. This is known as the no-profit rule. This includes situations where the directors use corporate property, information or opportunities without the permission of the company. The fact that a company cannot procure the transaction due to its financial inability does not justify the director profiting from the company's inability.

[78] *Industrial Development Consultants Ltd v. Cooley* [1972] 2 All ER 162 acts as a precedent. In this case, Cooley, the director of IDC, who was negotiating with the Gas Board on behalf of IDC, was offered the contract. The Gas Board did not want to award the contract to IDC. Cooley informed IDC that the Gas Board did not want to award the contract to IDC. He informed IDC of the Gas Board's decision but did not disclose to IDC that the offer was made to him. He subsequently resigned from IDC and took up the contract. IDC sued him for breach of his fiduciary duty for an account of the profits he had made. Cooley contended that the contract did not belong to IDC as the Gas Board did not want to award the contract to it.

(1) While the defendant was managing director of the plaintiffs a fiduciary relationship existed between him and the plaintiffs; accordingly information which came to him while he was managing director and was of concern to the plaintiffs, was information which it was his duty to disclose to the plaintiffs. He was under a duty therefore to disclose all information which he received in the course of his dealings with the gas board. Instead he had embarked on a deliberate course of conduct which had put his personal interests as a potential contracting party with the gas board in direct conflict with his pre-existing and continuing duty as managing director of the plaintiffs. He was therefore in breach of his fiduciary duty to the plaintiffs in failing to pass on to them all the relevant information received in the course of his dealings with the gas board and in guarding it for his own personal purposes and profit.

(2) Because of his breach of duty the defendant was liable to account to the plaintiffs for all the benefit he had received or would receive under the contract with the gas board. The question whether the benefit of the contract would have been obtained for the plaintiffs but for the defendant's breach of fiduciary duty was irrelevant. It was therefore irrelevant that, as a result of the order to account, the plaintiffs would receive a benefit which they would not otherwise have received.

[79] In the case of *PJTV Denson (M) Sdn Bhd & Ors v. Roxy (Malaysia) Sdn Bhd* [1980] 1 LNS 55; [1980] 2 MLJ 136, the company could not complete the agreement for the purchase of the land due to shortage of funds. As such, the land was purchased by two directors of the company.

"Again directors are called trustees. They are no doubt trustees of assets which have come to their hands or which are under their control" – (per Sir George Jessel MR in *In Re Forest of Dean Coal Mining Co*). As trustees they could not purchase the said land. The inflexible rule of equity forbade them to do that ... They no doubt could purchase only with the knowledge and consent of their *cestui que* trust. In the absence of such knowledge and consent they are accountable: see *Keech v. Sandford* and *Regal (Hastings) Ltd v. Gulliver*.

The allegation that the company lacked funds to purchase and that the second and third appellants bought the land with their own money as members of the public is a travesty of the facts. The same argument was raised and rejected in *Regal (Hastings) Ltd v. Gulliver*. Lord Russel of Killowen said (at page 149): "It was contended that it was impossible for Regal to get the shares owing to lack of funds and that the directors in taking the shares were really acting as members of the public. We cannot accept this argument ...".

[80] By way of the derivative action, the first defendant is entitled to seek, *inter alia*, an account of the profits made by the second defendant.

A **Conclusion**

[81] This court is satisfied as below:

(i) The plaintiff has satisfied all the pre-conditions for obtaining leave to commence a derivative action. He has *locus standi* to do so. He is acting in good faith and the derivative action is for the best interests of the first defendant. His action is not frivolous or vexatious.

(ii) There exists reasonable prospect for success in the anticipated derivative action. There is also reasonable and legitimate basis for bringing a derivative action to recover the loss of income which belongs to the first defendant.

(iii) Based on the facts and case authorities stated above, it is clear that the plaintiff has a case for averring that the second defendant has breached his fiduciary duties to the company (the first defendant) in incorporating the third defendant and in diverting the business and business opportunities to the third defendant, in which he was at all material times the shareholder and director. If a loss of income arose from a breach of fiduciary duty on the part of a director, it would be in the interests of the company to take steps to recover such income.

(iv) The existence of financial benefit which the director has obtained personally through other companies, firms or business can be used to show that there is conflict of interest and duty. A director owes a responsibility not to hide his interest or involvement in a transaction where the transaction is entered into by him for and on behalf of a third party in which he has an interest and the said third party competes with the company in respect of the business carried out by the company.

(v) The plaintiff filed Originating Summons No: PA-24NCVC-193-03-2017 to apply for an injunction in order to secure the data and prevent the second defendant from erasing important information which was critical to the case at that time. The High Court dismissed the plaintiff's application for an interim injunction based on a technical issue and not on merits. The High Court also struck out the plaintiff's application for leave for committal proceedings against the second defendant as the plaintiff had decided not to proceed with the committal proceedings with the OS having been struck out.

(vi) The Court of Appeal struck out the plaintiff's appeals as the plaintiff withdrew the appeals on the understanding that there was a technical error regarding the section under which the said OS was filed. Merits of the case was not ventilated or decided by the court.

I Based on those deliberations encl. 1 is hereby allowed.